

AMENDED IN SENATE AUGUST 22, 2008  
AMENDED IN ASSEMBLY JANUARY 7, 2008  
AMENDED IN ASSEMBLY APRIL 10, 2007

CALIFORNIA LEGISLATURE—2007–08 REGULAR SESSION

**ASSEMBLY BILL**

**No. 1012**

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**Introduced by Assembly Member Charles Calderon**

February 22, 2007

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An act to amend ~~Section 276 of~~ *Sections 24411 and 25110 of, and to add Section 25117 to, the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.*

LEGISLATIVE COUNSEL'S DIGEST

AB 1012, as amended, Charles Calderon. ~~Property tax exemption: disabled veterans.~~ *Corporation tax law: water's edge.*

*Existing law provides that, in the case of a business with income derived from, or attributable to, sources both within and without this state, the income is apportioned between this state and other states and foreign countries for tax purposes in accordance with a specified formula based on the property, payroll, and sales within and without this state, except as otherwise provided. Existing law permits certain taxpayers, as provided, to elect to determine their income under a water's edge election and specifies certain requirements under that election.*

*This bill would conform specified provisions relating to, among other things, the water's edge election to specified federal income tax laws relating to the taxation of certain shareholders of controlled foreign corporations, as provided.*

*This bill would take effect immediately as a tax levy.*

~~Existing property tax law provides, pursuant to the authorization of the California Constitution, for the exemption from property taxation of specified amounts of the assessed value of the home of a disabled veteran, or a veteran's spouse in the case in which the person has, as a result of a service-connected disease or injury, died while on active duty in military service.~~

~~This bill would correct an erroneous cross-reference and remove obsolete references to prior exemption amounts.~~

Vote: majority. Appropriation: no. Fiscal committee: ~~no~~ yes.  
State-mandated local program: no.

*The people of the State of California do enact as follows:*

- 1     SECTION 1. Section 24411 of the Revenue and Taxation Code  
2     is amended to read:  
3     24411. (a) For purposes of those taxpayers electing to compute  
4     income under Section 25110, ~~100 percent of the qualifying~~  
5     ~~dividends described in subdivision (c) and 75 percent of other~~  
6     ~~qualifying dividends to the extent not otherwise allowed as a~~  
7     ~~deduction or eliminated from income. "Qualifying dividends"~~  
8     ~~means those received by the water's-edge group from corporations~~  
9     ~~if both of the following conditions are satisfied to the extent not~~  
10    ~~otherwise allowed as a deduction or eliminated from income:~~  
11    (1) *One hundred percent of the qualifying dividends described*  
12    ~~in subdivision (d).~~  
13    (2) *Twenty-seven percent of qualifying dividends described in*  
14    ~~Section 25117.~~  
15    (3) *Seventy-five percent of qualifying dividends, other than those*  
16    ~~referred to in paragraph (1) or (2).~~  
17    (b) *"Qualifying dividends" means those received by the*  
18    ~~water's-edge group from corporations if both of the following~~  
19    ~~conditions are satisfied:~~  
20    (1) *The average of the property, payroll, and sales factors within*  
21    ~~the United States for the corporation is less than 20 percent.~~  
22    (2) *More than 50 percent of the total combined voting power*  
23    ~~of all classes of stock entitled to vote is owned directly or indirectly~~  
24    ~~by the water's-edge group.~~  
25    ~~(b)~~

1 (c) The water's-edge group consists of corporations whose  
2 income and apportionment factors are taken into account pursuant  
3 to Section 25110.

4 (e)

5 (d) Dividends derived from a construction project, the location  
6 of which is not subject to the taxpayer's control.

7 For purposes of this subdivision:

8 (1) "Construction project" means any activity which meets the  
9 following requirements:

10 (A) Is undertaken for any entity, including a governmental  
11 entity, which is not affiliated with the taxpayer.

12 (B) The majority of its cost of performance is attributable to an  
13 addition to real property or an alteration of land or any  
14 improvement thereto as those terms are utilized for purposes of  
15 this code.

16 "Construction project" does not include the operation, rental,  
17 leasing, or depletion of real property, land, or any improvement  
18 thereto.

19 (2) "Location of which is not subject to the taxpayer's control"  
20 means that the place at which the majority of the construction takes  
21 place results from the nature or character of the construction project  
22 and not as a result of the terms of the contract or agreement  
23 governing the construction project.

24 *SEC. 2. Section 25110 of the Revenue and Taxation Code, as*  
25 *added by Section 2 of Chapter 22 of the Statutes of 2006, is*  
26 *amended to read:*

27 25110. (a) Notwithstanding Section 25101, a qualified  
28 taxpayer, as defined in paragraph (2) of subdivision (b), that is  
29 subject to the tax imposed under this part, may elect to determine  
30 its income derived from or attributable to sources within this state  
31 pursuant to a water's-edge election in accordance with the  
32 provisions of this part, as modified by this article. A taxpayer, that  
33 makes a water's-edge election on or after January 1, 2006, shall  
34 take into account that portion of its own income and apportionment  
35 factors and the income and apportionment factors of its affiliated  
36 entities to the extent provided below:

37 (1) The entire income and apportionment factors of any of the  
38 following corporations:

39 (A) Domestic international sales corporations, as described in  
40 Sections 991 to 994, inclusive, of the Internal Revenue Code and

1 foreign sales corporations as described in Sections 921 to 927,  
2 inclusive, of the Internal Revenue Code.

3 (B) Any corporation (other than a bank), regardless of the place  
4 where it is incorporated if the average of its property, payroll, and  
5 sales factors within the United States is 20 percent or more.

6 (C) Corporations that are incorporated in the United States,  
7 excluding corporations making an election pursuant to Sections  
8 931 to 936, inclusive, of the Internal Revenue Code.

9 (D) Export trade corporations, as described in Sections 970 to  
10 972, inclusive, of the Internal Revenue Code.

11 (2) ~~(A) With respect to a corporation that is not described in~~  
12 ~~subparagraphs (A), (B), (C), and (D) of paragraph (1), as provided~~  
13 ~~in either one or both of the following clauses:~~

14 ~~(i) The~~ *the* income and apportionment factors of that corporation  
15 to the extent of its income derived from or attributable to sources  
16 within the United States and its factors assignable to a location  
17 within the United States in accordance with paragraph (3) of  
18 subdivision (b). Income of that corporation derived from or  
19 attributable to sources within the United States as determined by  
20 federal income tax laws shall be limited to, and determined from,  
21 the books of account maintained by the corporation with respect  
22 to its activities conducted within the United States.

23 ~~(ii) The income and apportionment factors of that corporation~~  
24 ~~that is a “controlled foreign corporation,” as defined in Section~~  
25 ~~957 of the Internal Revenue Code, to the extent determined by~~  
26 ~~multiplying the income and apportionment factors of that~~  
27 ~~corporation without application of this subparagraph by a fraction~~  
28 ~~not to exceed one, the numerator of which is the “Subpart F~~  
29 ~~income” of that corporation for that taxable year and the~~  
30 ~~denominator of which is the “earnings and profits” of that~~  
31 ~~corporation for that taxable year.~~

32 (B) For purposes of this paragraph, both of the following apply:

33 (i) “Subpart F income” means “Subpart F income” as defined  
34 in Section 952 of the Internal Revenue Code.

35 (ii) “Earnings and profits” means “earnings and profits” as  
36 described in Section 964 of the Internal Revenue Code.

37 (3) The income and apportionment factors of the corporations  
38 described in this subdivision shall be taken into account only to  
39 the extent that they would have been taken into account had no  
40 election under this section been made.

1     ~~(4) The Franchise Tax Board shall prescribe regulations to~~  
2     ~~coordinate implementation of subparagraph (A) of paragraph (2)~~  
3     ~~to prevent multiple inclusion or exclusion of income and factors~~  
4     ~~in situations where the same item of income is described in both~~  
5     ~~clauses.~~

6     (b) For purposes of this article and Section 24411, all of the  
7     following definitions apply:

8     (1) An “affiliated corporation” means a corporation that is a  
9     member of a commonly controlled group as defined in Section  
10    25105.

11    (2) A “qualified taxpayer” means a corporation that does both  
12    of the following:

13    (A) Files with the state tax return, on which the water’s-edge  
14    election is made, a consent to the taking of depositions, at the time  
15    and place most reasonably convenient to all parties, from key  
16    domestic corporate individuals and to the acceptance of subpoenas  
17    duces tecum requiring reasonable production of documents to the  
18    Franchise Tax Board, as provided in Section 19504, by the State  
19    Board of Equalization, as provided in Section 5005 of Title 18 of  
20    the California Code of Regulations, or by the courts of this state,  
21    as provided in Chapter 2 (commencing with Section 1985) of Title  
22    3 of Part 4 of, and Chapter 9 (commencing with Section 2025.010)  
23    of Title 4 of Part 4 of, the Code of Civil Procedure. The consent  
24    relates to issues of jurisdiction and service and does not waive any  
25    defenses that a taxpayer may otherwise have. The consent shall  
26    remain in effect as long as the water’s-edge election is in effect,  
27    and shall be limited to providing that information necessary to  
28    review or adjust income or deductions in a manner authorized by  
29    Section 482, 861, Subpart F of Part III of Subchapter N, or similar  
30    provisions, of the Internal Revenue Code, together with the  
31    regulations adopted pursuant to those provisions, and for the  
32    conduct of an investigation with respect to any unitary business  
33    in which the taxpayer may be involved.

34    (B) Agrees that, for purposes of this article, dividends received  
35    by any corporation whose income and apportionment factors are  
36    taken into account pursuant to subdivision (a) from either of the  
37    following are functionally related dividends and shall be presumed  
38    to be business income:

1 (i) A corporation of which more than 50 percent of the voting  
2 stock is owned, directly or indirectly, by members of the unitary  
3 group and which is engaged in the same general line of business.

4 (ii) Any corporation that is either a significant source of supply  
5 for the unitary business or a significant purchaser of the output of  
6 the unitary business, or that sells a significant part of its output or  
7 obtains a significant part of its raw materials or input from the  
8 unitary business. "Significant," as used in this subparagraph, means  
9 an amount of 15 percent or more of either input or output.

10 All other dividends shall be classified as business or nonbusiness  
11 income without regard to this subparagraph.

12 (3) The definitions and locations of property, payroll, and sales  
13 shall be determined under the laws and regulations that set forth  
14 the apportionment formulas used by the individual states to assign  
15 net income subject to taxes on, or measured by, net income in that  
16 state. If a state does not impose a tax on, or measured by, net  
17 income or does not have laws or regulations with respect to the  
18 assignment of property, payroll, and sales, the laws and regulations  
19 provided in Article 2 (commencing with Section 25120) shall  
20 apply.

21 Sales shall be considered to be made to a state only if the  
22 corporation making the sale may otherwise be subject to a tax on,  
23 or measured by, net income under the Constitution or laws of the  
24 United States, and shall not include sales made to a corporation  
25 whose income and apportionment factors are taken into account  
26 pursuant to subdivision (a) in determining the amount of income  
27 of the taxpayer derived from or attributable to sources within this  
28 state.

29 (4) "The United States" means the 50 states of the United States  
30 and the District of Columbia.

31 (c) All references in this part to income determined pursuant to  
32 Section 25101 shall also mean income determined pursuant to this  
33 section.

34 *SEC. 3. Section 25117 is added to the Revenue and Taxation*  
35 *Code, to read:*

36 *25117. (a) Except as otherwise provided, income taken into*  
37 *account by all affiliated entities whose income and apportionment*  
38 *factors are determined pursuant to Section 25110 shall include*  
39 *income described in Subpart F of the Internal Revenue Code*  
40 *(commencing with Section 951). The income that is taken into*

1 *account shall for all purposes be treated as a dividend actually*  
2 *paid, and be subject to any provision or limitation related to the*  
3 *treatment of dividends, including, but not limited to, Sections*  
4 *24344, 24410, 24411, and 25106. The amount taken into account*  
5 *shall be treated as business or nonbusiness income as defined in*  
6 *Section 25120, as the case may be.*

7 *(b) In the application of Subpart F of the Internal Revenue Code:*

8 *(1) Exclusions from gross income under Section 959 of the*  
9 *Internal Revenue Code, relating to previously taxed income, shall*  
10 *apply, including amounts related to income previously taxed under*  
11 *federal law in years prior to the water's-edge election.*

12 *(2) Federal adjustments to stock basis made pursuant to Section*  
13 *961 of the Internal Revenue Code, relating to adjustments to basis*  
14 *of stock in controlled foreign corporations and of other property,*  
15 *including adjustments made prior to the water's-edge election,*  
16 *shall apply.*

17 *(3) The provisions of and any reference to Section 1248 of the*  
18 *Internal Revenue Code, relating to gain from certain sales or*  
19 *exchanges of stock in certain foreign corporations, shall not apply.*

20 *(4) Section 960 of the Internal Revenue Code, relating to special*  
21 *rules for foreign tax credit, shall not apply.*

22 *(5) Section 965 of the Internal Revenue Code, relating to*  
23 *temporary dividends received deduction, shall not apply.*

24 *(6) For purposes of this section, a federal election to exclude*  
25 *from Subpart F income the income described in Section 954(b)(4)*  
26 *of the Internal Revenue Code shall apply, including amounts*  
27 *related to income previously taxed under federal law in years prior*  
28 *to the water's-edge election. No election under this subparagraph*  
29 *shall be allowed for state purposes unless a valid election was*  
30 *made for federal purposes.*

31 *(c) In the event that a water's-edge election is terminated, for*  
32 *taxable years thereafter, the following rules apply:*

33 *(1) Subpart F of the Internal Revenue Code shall not apply,*  
34 *except as provided in this subdivision.*

35 *(2) Section 959 of the Internal Revenue Code, relating to*  
36 *exclusion from gross income of previously taxed earnings and*  
37 *profits, shall apply, but only to the extent attributable to income*  
38 *that has been taken into account pursuant to subdivision (a) during*  
39 *the period of the water's-edge election.*

1     (3) *Stock basis shall be determined as if this section did not*  
2 *apply, except that stock basis shall be:*

3     (A) *Increased by income taken into account pursuant to*  
4 *subdivision (a) during the period of the water's-edge election.*

5     (B) *Reduced by both the following:*

6     (i) *That portion of amounts excluded from income under*  
7 *paragraph (2) of subdivision (b) that are attributable to income*  
8 *taken into account pursuant to subdivision (a) during the period*  
9 *of the water's-edge election.*

10    (ii) *Amounts described by paragraph (2) of subdivision (c)*  
11 *excluded from income after termination of the water's-edge*  
12 *election.*

13    (d) (1) *Except as provided in paragraph (2), this section shall*  
14 *apply to taxable years beginning on or after January 1, 2008.*

15    (2) *In the event that two or more taxpayers subject to the same*  
16 *election under Section 25110 have different taxable years, this*  
17 *section shall apply as of the first day of the first taxable year of*  
18 *those respective taxpayers that begins on or after January 1, 2008.*

19    (e) *If a distribution with respect to earnings and profits from a*  
20 *given year is eligible for treatment as previously taxed income and*  
21 *would, without regard to the application of this section, be eligible*  
22 *for deduction, exclusion, or elimination under another section*  
23 *under this part, if paid as a dividend, in no event shall the*  
24 *combined effect of those sections and the rules relating to*  
25 *previously taxed income result in a deduction, exclusion, or*  
26 *elimination greater than the amount of the earnings and profits*  
27 *that apply to the distribution.*

28    (f) *Subdivision (a) of Section 24425 shall not apply to amounts*  
29 *excluded from gross income pursuant to this section or to amounts*  
30 *deducted pursuant to paragraph (2) of subdivision (a) of Section*  
31 *24411.*

32    (g) *The Franchise Tax Board may prescribe regulations as may*  
33 *be necessary and appropriate to carry out the purposes of this*  
34 *section.*

35    SEC. 4. *This act provides for a tax levy within the meaning of*  
36 *Article IV of the Constitution and shall go into immediate effect.*  
37 *However, except as otherwise provided, this act shall apply to*  
38 *taxable years beginning on or after January 1, 2008.*

39    ~~SECTION 1. Section 276 of the Revenue and Taxation Code~~  
40 ~~is amended to read:~~



1     ~~276. (a) Except as otherwise provided by subdivision (b), for~~  
2 ~~property for which the disabled veterans' exemption described in~~  
3 ~~Section 205.5 was available, but for which a timely claim was not~~  
4 ~~filed, a partial exemption shall be applied in accordance with~~  
5 ~~whichever of the following is applicable:~~

6     ~~(1) Ninety percent of any tax, including any interest or penalty~~  
7 ~~thereon, levied upon that portion of the assessed value of the~~  
8 ~~property that would have been exempt under a timely and~~  
9 ~~appropriate claim shall be canceled or refunded, provided that an~~  
10 ~~appropriate claim for exemption is filed after 5 p.m. on February~~  
11 ~~15 of the calendar year in which the fiscal year begins but on or~~  
12 ~~before the following December 10.~~

13     ~~(2) If an appropriate claim for exemption is filed after the time~~  
14 ~~period specified in paragraph (1), 85 percent of that portion of any~~  
15 ~~tax, including any interest or penalty thereon, that was levied upon~~  
16 ~~that portion of the assessed value of the property that would have~~  
17 ~~been exempt under a timely and appropriate claim, shall be~~  
18 ~~canceled or refunded. Cancellations made under this paragraph~~  
19 ~~are subject to the provisions of Article 1 (commencing with Section~~  
20 ~~4985) of Chapter 4. Refunds issued under this paragraph are subject~~  
21 ~~to the limitations periods on refunds as described in Article 1~~  
22 ~~(commencing with Section 5096) of Chapter 5.~~

23     ~~(b) If a late filed claim for the one-hundred-fifty-thousand-dollar~~  
24 ~~(\$150,000) exemption is filed in conjunction with a timely filed~~  
25 ~~claim for the one-hundred-thousand-dollar (\$100,000) exemption,~~  
26 ~~the amount of any exemption allowed under the late-filed claim~~  
27 ~~under subdivision (a) shall be determined on the basis of that~~  
28 ~~portion of the exemption amount, otherwise available under~~  
29 ~~subdivision (a), that exceeds one hundred thousand dollars~~  
30 ~~(\$100,000), as applicable.~~

31     ~~(c) For those claims filed pursuant to subdivision (a) after~~  
32 ~~November 15, the exemption under that subdivision may be applied~~  
33 ~~to the second installment. If that exemption is so applied, the first~~  
34 ~~installment is still delinquent on December 10, and is subject to~~  
35 ~~delinquent penalties provided for in this division if that installment~~  
36 ~~is not timely paid. A refund shall be made to the taxpayer upon a~~  
37 ~~claim submitted to the auditor if the exemption is applied to the~~  
38 ~~second installment and either of the following is true:~~

39     ~~(1) Both installments are paid on or before December 10.~~

- 1     ~~(2) The reduction in taxes resulting from the exemption exceeds~~
- 2     ~~the amount of taxes due on the second installment.~~

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